THE CITY OF SAN DIEGO

Redevelopment Agency's Report

DATE ISSUED: October 6, 2004 REPORT NO. RA-04-34

ATTENTION: Chair and Members of the Redevelopment Agency
Docket of October 12, 2004

SUBJECT: Third Implementation Agreement to the Disposition and Development Agreement for the North Park Theatre Rehabilitation Project

SUMMARY:

Issues –

1) Should the Redevelopment Agency Approve the Third Implementation Agreement to the Disposition and Development Agreement (DDA) North Park Theatre, LLC for the North Park Theatre Rehabilitation Project?
2) Should the Redevelopment Agency Amend the Fiscal Year 2005 Redevelopment Agency Budget for the North Park Project Area to Increase Appropriations and Authorize Expenditures in the Amount of $40,000 from North Park Series 2003 Bond Proceeds (Taxable) for the North Park Theatre Project (Fund 98309).

Executive Director Recommendation –

1) Approve the Third Implementation Agreement to the DDA with North Park Theatre, LLC for the North Park Theatre Rehabilitation Project.
2) Amend the Fiscal Year 2005 Redevelopment Agency Budget for the North Park Project Area to Increase Appropriations and Authorize Expenditures in the Amount of $40,000 from North Park Series 2003 Bond Proceeds (Taxable) for the North Park Theatre Project (Fund 98309).

Fiscal Impact – Total rehabilitation costs are estimated to be approximately $7,167,000 and will be funded by North Park Theatre, LLC. A loan to the Agency from North Park Theatre, LLC will fund the Agency's subsidy of $3,335,000 for the rehabilitation. Loan payments will be made from new tax increment received by the Agency within the North Park Redevelopment Project Area, proceeds of a future tax allocation bond sale for North Park, other funds lawfully available to the Agency for such purpose, or proceeds from the sale of Agency-owned land. Interest on the outstanding balance of the total Agency reimbursement obligation will accrue to North Park Theatre, LLC at a variable rate of prime plus 2% per year until rehabilitation is completed, at which time the interest rate will escalate by one-half percentage point per year, but shall not exceed prime plus 4%. Quarterly interest-only payments, resulting in annual payments ranging from $140,696 in the first year of the agreement (based on a Prime Rate of 4.75% as quoted on September 21, 2004) and potentially exceeding $275,136 in the fifth year, will be made while an outstanding balance remains. Repayment of principal will be made as unallocated tax increment receipts permit. The Agency has the option to pledge new tax increment receipts in a bond sale and use the proceeds to repay the outstanding balance in full without prepayment penalty. The remainder of the project budget will be funded by North Park Theatre, LLC.

Environmental Impact – A Final Environmental Impact Report analyzing the probable effects of development activity implementing the North Park Redevelopment Project was adopted in January of 1997 (SCH No. 93-121105). Pursuant to the State Guidelines for the Implementation of the California Environmental Quality Act (CEQA) (California Administrative Code, Section 15000 et. seq.) and the San Diego Redevelopment Agency's amended "Procedures for Implementation of CEQA and the State CEQA Guidelines" (adopted July 17, 1990), an Environmental Secondary Study analyzing the probable impacts of the theatre renovation project certified by the Redevelopment Agency and City Council on April 23, 2002 (R-03460). The Environmental Secondary Study identifies no probable activity-specific environmental effects beyond those identified in the Final Environmental Impact Report (EIR) for the North Park Redevelopment Project. Mitigation measures identified in the North Park Redevelopment Project EIR and applicable to the proposed activity are listed in Attachment A of the Secondary Study.

Traffic Impacts
The project is fully permitted. Approval of the Second Implementation Agreement will result in no new traffic impacts.

BACKGROUND:

Subject to a Disposition and Development Agreement (DDA) with Arnold "Bud" Fischer, doing business as North Park Theatre, LLC (Developer) adopted on April 23, 2002, the Redevelopment Agency has performed a seismic retrofit of the historic North Park Theatre and conveyed the property to Mr. Fischer, who will perform interior and exterior tenant improvements with the intent of reopening the theatre in October of 2005 as a modern live-performance venue, visually consistent with the Theatre's 1928 appearance. The completed project will include an 800-seat performance space, a 5,800 square foot restaurant, and 6,700 square feet of leaseable office space. It is Mr. Fischer's intent to lease the renovated theatre to Lyric Opera San Diego on a long term basis. The lease would grant Lyric Opera San Diego the option of purchasing the entire facility on predetermined terms. Lyric Opera San Diego has been successful in generating pledges of $1,800,000 toward the purchase of the theatre.

The First Implementation Agreement to the DDA for the theatre rehabilitation (May 2, 2003) extended the time allowed for completion of the Agency seismic retrofit and conveyance to the Developer.

The Second Implementation Agreement (April 28, 2004) authorized the Executive Director to execute a loan of $3,300,000 from the Developer to the Redevelopment Agency as an additional subsidy to the project needed to fill a funding gap resulting from previously undetected deficiencies in the property, higher building and historic renovation standards, enhanced theatre production capacities, additional environmental testing and mitigation, labor costs and price inflation. The loan of $3,300,000 from the Developer to the Redevelopment Agency is to be repaid from future receipts of unallocated tax increment or other available sources and provided no schedule of repayment, with interest on the outstanding balance at a rate of 5%. The terms of the Second Implementation Agreement also restrict the use of the theatre auditorium such that it cannot be physically rededicated to a non-performance purpose for a period of fifty years from the date of execution of the agreement.

At the adoption of the Second Implementation Agreement, estimates for the cost of theatre improvements and equipment consistent with a first-class performing arts facility totaled $6,237,000. Together with renovation of the office and restaurant spaces fronting on University Avenue, the total property renovation cost was estimated at $7,132,000.

DISCUSSION:

During the Redevelopment Agency's seismic retrofit and removal of hazardous material from the theatre property, Agency staff worked with the City's Environmental Services and Water Departments to resolve an ongoing problem of water intrusion. Moisture was evident throughout the property, contributing to the growth of mold and collecting in the under-stage dressing areas. The replacement of the theatre's roof improved conditions substantially but failed to eliminate soil moisture. Several investigations, including a nighttime survey of underground pipes and valves using a sonar device to detect leaking water, proved inconclusive. In the absence of an identifiable source, it was determined that a foundation drain should be installed to intercept ground water along the south and west boundaries of the property. The cost of this measure was included in the budget approved with the Second Implementation Agreement to the DDA.

Following conveyance of the property to Mr. Fischer, additional moisture has been observed rising in cracks in the concrete slab of the retail spaces facing University Avenue. In order to mitigate this intrusion, it is proposed that the slab be coated with sealant. Also observed upon the initiation of the Developer's renovations, was a substantial leak in an abandoned fire service lateral in the public right-of-way adjacent to the building along 29th Street. The Developer obtained approval to cut and cap this lateral, incurring the additional costs of labor, equipment and permitting fees.

The additional rehabilitation costs incurred by the Developer relating to water infiltration from various off-site sources total $35,000 under the terms of the proposed Third Implementation Agreement (Attachment 1). It is proposed that the Redevelopment Agency authorize the Developer to increase the amount of the Agency's loan by this amount, to be repaid from future unallocated tax increment receipts. Investigations of moisture intrusion have contributed to Agency costs in excess of budgeted levels. Because of this, it is recommended that additional funds in the amount of $40,000 be authorized for expenditure by the Agency for this project. As shown in the chart below, funds are available from the North Park Series 2003 taxable bond proceeds for this purpose.

~~CITY OF SAN DIEGO~~
~~M E M O R A N D U M~~

~~DATE: December 4, 2003~~

~~TO: Honorable Chair and Members of the Redevelopment Agency~~

~~FROM: Hank Cunningham, Assistant Executive Director~~

~~SUBJECT: Bond Sale Results~~

STATUS OF NORTH PARK BOND PROCEEDS			
	General Uses	Housing Uses	Total
Beginning Balance (inc. interest)	$13,882,840	$4,606,739	$18,489,579
Less Approved Projects:			
North Park Theatre	$2,080,000		
North Park Public Parking Lot	$1,840,000		
North Park Parking Structure	$8,338,000		
Renaissance at North Park		$3,954,500	
North Park -Main Street	$250,000		
30th Street Lighting	$90,000		
North Park Theatre Cost Increase	**$40,000**		
Subtotal Approved Projects	**$12,638,000**	**$3,954,500**	$16,592,500
Remaining Balance	$1,244,840	$652,239	$1,897,079

It is anticipated that requests to allocate the remaining balance of North Park Bond Proceeds will be coming forward for review and approval by the Redevelopment Agency over the course of the next few months.

~~The Redevelopment Agency of the City of San Diego accepted competitive bids today for the sale of four series of tax allocation bonds for the North Park and City Heights Redevelopment project areas. The following bids were received, with the winning bids shown in bold:~~

~~Bond Series~~	~~Par Amount~~	~~Underwriting Firm~~	~~True Interest Cost~~
~~NP Taxable~~	~~$7,145,000~~	~~**Morgan KeeganStanley**~~	~~**5.8655 %**~~
		~~Stone & Youngberg~~	~~6.0692 %~~
		~~Citigroup~~	~~6.1627 %~~
~~CH Taxable~~	~~$4,800,000~~	~~None~~	
~~CH Tax-Exempt~~	~~$865,000~~	~~**Stone & Youngberg**~~	~~**3.7449%**~~

~~NP Tax-Exempt~~	~~$5,360,000~~	~~**Citigroup**~~	~~**4.9400 %**~~
		~~UBS Financial ServicesPaine Webber~~	~~4.9435 %~~
		~~Stone & Youngberg~~	~~4.9766 %~~
		~~First Albany~~	~~5.0633 %~~

~~The winning bids were favorable, and in the range of costs anticipated by the Agency. The City Heights tax-exempt bonds received only one bid due to the small size of the issue and because the bonds were unable to qualify for bond insurance. The one bid received was favorable and, thus, accepted. No bids were received for the City Heights taxable bonds., though interest had been expressed by several underwriting firms in advance of the sale. The lack of bond insurance for the City Heights bonds, and the Agency's parameters for limits on the maximum allowable bid precluded the acceptance of those that were submitted during the electronic bidding process. Because of this, Tthe Agency has rescheduled the sale of the City Heights taxable bonds for Tuesday, December 9, and will permit the receipt of bids with higher rates of interest. The Agency has reason to believe that acceptable bids will be submitted, allowing for the successful sale of the bonds. The results of the City Heights taxable bond Tuesday's bond sale will be made available as soon as possible as soon as possible.~~

~~Hank Cunningham~~

Mr. Fischer also requests revisions to the terms of repayment of his loan to the Redevelopment Agency. These include the calculation of interest as an escalating spread over the prime rate, beginning at prime plus 2% and increasing after the first two years by 50 basis points each year during which a balance remains outstanding, not to exceed prime plus 4%. Under the terms of the Second Implementation Agreement, simple interest of 5% accrues on the outstanding balance, with no payment due until unallocated tax increment receipts are realized. The revised terms remain non-amortizing, but will require quarterly interest payments beginning 90 days following initiation of the Developer's renovation activities on August 1st, 2004. The method of imputing the value of the outstanding loan will be revised to stipulate that the Developer's loan is disbursed in 12 equal increments on a monthly basis for a period of one year following initiation of renovation activities. The method established in the Second Implementation Agreement assumes that the Developer's loan is disbursed in four quarterly increments over one year.

As authorized in the DDA for the theatre's rehabilitation, the Redevelopment Agency has purchased property located immediately south of the theatre to provide additional parking, particularly during construction of the parking garage to be located across 29th Street to the east. The Third Implementation Agreement provides that in the event the Redevelopment Agency sells this property while an outstanding balance remains on the Developer's loan to the Agency, the proceeds of the sale will be used, in part or in whole, to reduce the principal balance of the loan.

A comparison of financing costs associated with the developer's loan to the Redevelopment Agency under current agreements and under the proposed Third Implementation Agreement is provided in Attachment 2. The cost comparison – which holds the Prime Rate constant and assumes retirement of the debt through refinancing and/or the sale of Agency assets after 5 years - illustrates the potential cost of the proposed loan terms. Interest payments under the proposed Third Implementation Agreement would exceed those under the Second Implementation by $140,696 in the first year of the agreement and exceed $275,136 in the fifth year of the agreement, assuming that no principal payments are made over the five-year period. The additional financing cost can be expected to total at least $288,000. Increases in the Prime Rate, quoted at 4.75% on September 21, 2004, would increase the differential in financing costs. An earlier refinancing or sale of Agency assets would reduce the costs associated with the proposed loan terms. It is anticipated that the loan will be repaid within the next two to three years from the proceeds of a North Park tax allocation bond as additional revenues are generated within the project area.

Finally, the requirement for $2,000,000 in automobile insurance established in the Theatre Rehabilitation DDA will be reduced to $1,000,000.

ALTERNATIVE:

Do not approve the Third Implementation Agreement to the Disposition and Development Agreement for the North Park Theatre Rehabilitation Project.

Respectfully submitted,

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Debra Fischle-Faulk	Approved: Hank Cunningham
Deputy Executive Director	Assistant Executive Director

FAULK/TCR

Attachments:

1. Third Implementation Agreement with North Park Theatre, LLC for the North Park Theatre Rehabilitation Project
2. Third Implementation Agreement Comparison with the Cost of Funds Under Current Agreement

ATTACHMENT NO. 1

Third Implementation Agreement

with North Park Theatre, LLC

for the North Park Theatre Rehabilitation Project

Limited distribution.
Copies available for public review at the
Office of the City Clerk and Redevelopment Agency.